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In the Supreme Court of the United States

OCTOBER TERM, 1957

No. 923

PRESSED STEEL CAR COMPANY, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Court of Claims (Pet. App. 1–4) is reported at 157 F. Supp. 950. The court's findings of fact and conclusions of law (Pet. App. 4–22) are unreported.

JURISDICTION

The judgment of the Court of Claims dismissing the petition in that court was entered on January 15, 1958. The petition for a writ of certiorari was filed on April 15, 1958. The jurisdiction of this Court is invoked under 28 U. S. C. 1255 (1).

QUESTION PRESENTED

Whether Pennsylvania capital stock taxes, paid by a Pennsylvania corporation, are reimbursable under

a cost plus a fixed fee contract which was performed wholly in Illinois.

STATEMENT

This action was brought under the Tucker Act to recover, as allegedly reimbursable costs under a cost plus a fixed fee contract which was performed wholly in Illinois, certain Pennsylvania capital stock taxes paid by petitioner, a Pennsylvania corporation. The relevant facts may be summarized as follows:

On November 12, 1941, petitioner contracted with the Government to manufacture 900 M–4 tanks (F. 2)[1] at its Hegewisch, Illinois, plant, which the Government rehabilitated for petitioner (F. 3). Under the terms of the contract, petitioner was to be reimbursed by the Government for all direct costs and for "the proper proportion of any indirect cost . . . incident to and necessary for the performance of" the contract (F. 6, Art. IV, 1 (a) (1)). Property taxes, covering "property used for manufacturing purposes" in the performance of the contract were expressly included as "indirect" costs and were therefore pro rata reimbursable (F. 6, Art. IV, 1 (a) (3) (f) (iv)). On the other hand, federal and state income and excess profits taxes, and taxes on issues and transfers of capital stock, were expressly non-reimbursable costs (F. 6, Art. IV, 1 (a) (7) (d) (iii)).

The contract made no specific reference to the tax

[1] This prime contract was supplemented a number of times so that petitioner manufactured approximately 10,000 tanks prior to termination in 1945 (F. 3).

Court of Claims findings, which are reprinted in the Appendix to the Petition, will be cited by the number of the finding.

imposed by the state of Pennsylvania on the capital stock of, *inter alia,* corporations incorporated in that state, Purdon's Penna. Stat., Title 72, Ch. 2, Sections 1871–1903 (F. 8, 11). In computing this tax, the value of the capital stock of the corporation is determined by a number of formulae based on the average selling price of the stock, corporate earnings, and the "intrinsic value" of corporate assets (F. 11, 29). This value, which in petitioner's case was based partly on the earnings from its Government contract (F. 16), is then apportioned between "taxable" assets and "exempt" assets, one of which is tangible property located outside Pennsylvania. Therefore, petitioner's Hegewisch plant was exempted and a proportionate part of the value of the capital stock was relieved from taxation.

Although petitioner filed capital stock tax returns, and made payment of the tax, for the years 1941, 1942 and 1943, it never requested reimbursement until early in 1944, at which time it submitted claims for capital stock taxes as part of its general and administrative expenses for 1942 and 1943 (F. 19). On September 5, 1944, petitioner was advised by the Army that its claim was rejected (F. 19).

On June 1, 1945, the Government issued a notice of partial termination of the contract. The notice of complete termination followed on August 17, 1945, and on October 10, 1945, the Government terminated all research and development work effective December 31, 1945 (Def. Exh. 10, p. 3).

On July 2, 1946, the parties reached a termination settlement agreement, contained in a formal Termination Settlement Recommendation dated July 22,

1946, which excepted the Pennsylvania capital stock tax reimbursement matter from settlement pending a ruling of the Comptroller General (Def. Exh. 10, p. 8). This agreement, which was reiterated in Supplemental Settlement Agreement No. 104 of November 27, 1946 (F. 9), did not specify which of the parties was to apply for the ruling (*id.*, Art. 3 (c) (11)).

On September 26, 1946, two months before the Supplemental Settlement Agreement No. 104, the Comptroller General declined, for lack of jurisdiction, to decide whether certain gas-gathering taxes were reimbursable under a cost-plus-a-fixed-fee contract where the contract was already terminated (F. 22; 26 Comp. Gen. 216). The Office of the Chief of Ordnance in Washington, believing that this decision controlled petitioner's reimbursement claim, returned petitioner's voucher to the Chicago Ordnance District without submitting it to the Comptroller General (F. 22, 27). On February 9, 1948, the contracting officer denied petitioner's claim for reimbursement on the ground that "[i]nasmuch as the work was done outside of the taxing jurisdiction, the Pennsylvania Capital Stock Tax cannot be considered as being a charge allocable to this contract as being necessarily incident to the performance of such contract" (F. 23). Petitioner filed no administrative appeal from this denial (F. 23).

Petitioner thereupon filed its petition in the Court of Claims. The petition disclosed to the Government for the first time that petitioner believed that the Comptroller General had refused to decide whether

the Pennsylvania capital stock taxes were reimbursable costs. Since the question had never, in fact, been presented to the Comptroller General, the parties agreed to forward the claim to him before proceeding to trial. The Comptroller General, however, declined to take jurisdiction of the question (F. 28).

At trial, the Government introduced the testimony of the commanding officer of the Chicago Ordnance District in 1941, a member of the Chicago Ordnance District legal staff who had been one of the negotiators of the tank contract, and the Chief of the Legal Division of the Chicago Ordnance District at the time of the contract (R. 322, 358, 373). Each of these witnesses testified that he first heard of the Pennsylvania capital stock tax a few weeks prior to the trial in June, 1955 (R. 339, 361, 374). Petitioner introduced no testimony that the reimbursability of Pennsylvania capital stock taxes had been discussed during the negotiations for the contract.

The Court of Claims dismissed the petition (Pet. App. 1–4). Pointing to the fact that the capital stock tax paid by petitioner had been "based roughly upon that part of the market value of [its] stock which was created by the profits made by the operations of [its] plant in Pennsylvania and the value of the physical assets of [that] plant," the court determined that neither had a relation to the performance, or cost of the performance, of the contract with the Government (Pet. App. 3). It concluded (*ibid.*):

> It is not conceivable that if the parties, in negotiating the terms of the contract, had put their minds upon the question which faces us

here, and had analyzed the nature and operation of the Pennsylvania Capital Stock Tax, they would have agreed that it should be a reimbursable cost of the performance of the Illinois contract. The language of the contract is, at best, barely susceptible of an interpretation which would include this tax as a reimbursable cost. We should not so interpret it as to make a contract for the parties which, we are satisfied, they would not knowingly have made for themselves.

ARGUMENT

The court below has held that petitioner's contract with the Government did not entitle it to recover, as a reimbursable cost, its payment of the Pennsylvania capital stock tax. That holding, which rested upon the peculiar nature of the tax and the particular facts of the case, is clearly correct and presents no question of general importance. Moreover, there is no conflict of decisions. Accordingly, further review is not warranted.

1. As the court below observed, the Pennsylvania capital stock tax payments for which petitioner seeks reimbursement under its cost-plus-a-fixed-fee contract had no relation to the performance, in Illinois, of that contract. The Pennsylvania Supreme Court has repeatedly held that the capital stock tax is not a franchise or privilege tax but is, rather, a tax upon property or assets. See, *e. g.*, *Commonwealth* v. *Standard Oil Co.*, 101 Pa. 119; *Commonwealth* v. *Union Shipbuilding Co.*, 271 Pa. 403, 114 A. 257; *Commonwealth* v. *Southern Pennsylvania Bus Co.*, 339 Pa. 521, 15 A.

2d 375.[2] Referring to the *Standard Oil* decision, this Court itself has described the capital stock tax "as in substance and fact, though not in form, a tax specifically levied upon the property of the corporation." *Delaware, Lackawanna & Western R. Co.* v. *Pennsylvania,* 198 U. S. 341, 353, 356. And, the Pennsylvania court having also held that the tax is imposed only with respect to property which is located in Pennsylvania (*Commonwealth* v. *Union Shipbuilding Co., supra.*), the Illinois property employed by petitioner in carrying out the contract was exempt.

Since the Government negotiators were unaware of even the existence of the capital stock tax,[3] the contract did not make specific mention of it. It is nevertheless clear, as the court below determined, that had consideration been given to the tax it would not have been included as a reimbursable cost. Section 1 (a) (1), Article IV, of the contract provides that, in determining the cost of performance, "the proper proportion of any indirect costs * * * *incident to and necessary for* the performance of [the] contract" shall be allowed. (Emphasis added.) It follows from this provision that the Government did not contemplate the reimbursement of non-incidental expenditures such as the capital stock tax. There is, of course, no reason why reimbursement of such an expenditure would be contemplated.

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[2] Pennsylvania has a separate and distinct franchise tax "for the privilege of doing business in this Commonwealth." See Purdon's Penna. Stat., Title 72, Ch. 2, Sections 3420a–3420n.

[3] The contract was negotiated on the Government's behalf by the Chicago Ordnance District (R. 329), which does not encompass Pennsylvania (R. 324).

2. Petitioner's argument that *North American Aviation, Inc.* v. *United States*, 67 F. Supp. 1077, 107 C. Cls. 69, is inconsistent with the holding below is plainly without merit. In the first place, the *North American* case involved the federal capital stock tax "imposed upon every foreign corporation with respect to carrying on or doing business" (26 U. S. C. (1940 ed.) 1200 (b)).[4] It was thus, unlike the Pennsylvania tax, an excise levy imposed for the privilege of doing business, *i. e.*, a franchise tax. See *Flint* v. *Stone Tracy Co.*, 220 U. S. 107. As such, its payment was necessary to the performance of North American's contract and, therefore, was a reimbursable cost.

Moreover, the contract provisions and the background of the negotiations in *North American*, relied upon by the Court of Claims in that case, were markedly different from those here. The North American contract expressly incorporated Treasury Decision 5000 (Internal Revenue Cumulative Bulletin, 1940–2, p. 397), which determined that "excise taxes with respect to the carrying on or doing business * * * constitute proper reimbursable items of cost of performance of cost-plus contracts," 67 F. Supp. 1007 at 1015. Consequently, as the Court of Claims held, the parties had agreed in effect that the contractor was to obtain reimbursement of the federal tax. In this connection, the court found that "the parties * * * were fully

[4] Repealed by Revenue Act of November 8, 1945, Ch. 453, Sec. 201, 59 Stat. 574, effective with respect to years ending after June 30, 1945.

aware of the tax and * * * had at hand all the knowledge and means necessary to place a limitation on the reimbursement for the capital stock had they desired or intended that there be such a limitation," *id.* at 1017. As has been seen, this was not true in this case.

3. Nor is there merit to petitioner's reliance on the September 14, 1945, amendment to Army Technical Manual 14–1000 concerning the audit procedures for cost-plus-a-fixed-fee contracts. In the first place, since this amendment was not issued until four years after the contract was executed, it has no bearing upon the intent of the negotiators. Moreover, the amendment, which erroneously listed the Pennsylvania capital stock tax as a "state franchise tax levied for the privilege of doing business," *authorized* but did not *direct* reimbursement of state franchise taxes. Indeed, this distinction is pointed up by the digested decision in the November 1945, Bulletin of the Judge Advocate General of the Army (Vol. IV, No. 11, p. 469), relied on by petitioner (Pet. 14–15):

> *State franchise tax.*—Subject to the assumptions hereinafter expressed, *there is no objection to reimbursement*, in accordance with pars. 266 and 267, TM 14–1000, May 1945 [as added by C 2, 1 September 1945], of payments made by cost-plus-a-fixed-fee contractors on account of *true* State franchise taxes where payment of the tax is a necessary expense in connection with the performance of the contract and *where reimbursement is approved by the contracting officer.* * * * [Emphasis added.]

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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May 1958